JANUS CAPITAL Group

Investment Outlook

from Bill Gross

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Populism Takes a Wrong Turn

The Trumpian Fox has entered the Populist Henhouse, not so much by stealth but as a result of Middle America's misinterpretation of what will make America great again. Not having voted for either establishment party's candidate, I write in amazed, almost amused bewilderment at what American voters have done to themselves. A Reuters/Ipsos Election Day Survey of 10,000 voters revealed the extraordinary fury of the American populist movement. Almost 72% agreed that "the American economy is rigged to the advantage of the rich and powerful". Count me among them, yet in voting to deny Hillary Clinton the Henhouse, they "unwittingly" (lack of wit), let Donald Trump sneak in the side door. His tenure will be a short four years but is likely to be a damaging one for jobless and low-wage American voters. They were the force for Trump's flipping the Midwest into a Republican Electoral College victory. But while the Fox promised jobs and to make America great again, his policies of greater defense and infrastructure spending combined with lower corporate taxes to invigorate the private sector continue to favor capital versus labor, markets versus wages, and is a continuation of the status quo.

For example, Republican pleas for tax reform are centered around the argument that America has one of the highest corporate tax rates in the world at 35%. Not so. Of the S&P 500's largest 50 corporations, the average tax rate (including state, local and foreign regulations) is 24%. U.S. corporations rank among the world's most lightly, as opposed to heavily, taxed. Trump policies also appear to favor the repatriation of trillions of dollars of foreign profits at extremely low cost under the logic that the money will be spent for investment here in the U.S. Doubtful. The last time such a "pardon" was put into law in 2004, no noticeable pickup in investment took place. Of the $362 billion that earned a "tax holiday", most went to dividends, corporate bonuses, and stock buybacks. Apple or any other large U.S. corporation can borrow the money they need here in the U.S. at historically low interest rates to fund investment. A few have, but over $500 billion annually in recent years has gone to the repurchase of corporate stock and the increase of earnings per share, instead of earnings and GDP growth. Why would they need to repatriate anything for investment in the real economy?

But could a Clinton Administration have done much better? Probably not. Both the Clinton Democrats and almost all Republicans represent the corporate status quo that favors markets versus wages; Wall Street versus Main Street. That's why the American public and indeed global citizens will continually take a wrong turn in their efforts to neuter the establishment and to regain several decades' lost momentum in real wages versus real profits. Neither party as they now stand has bold policies beyond the reach of K Street Lobbyists. To my mind, there are better solutions than either party's election platform, such as a Keynesian/FDR job corps or a Kennedyesque AmeriCorps that puts people to work helping other people. Such programs were

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never emphasized by either candidate. Let's supplement welfare with a patriotic "Help America" jobs program, even if government organized. Would it be as efficient as a corporate-led effort? Of course not, but corporations are fighting structural headwinds, such as demographic aging, technological displacement of jobs (robotization), deglobalization, and overleveraged balance sheets. They focus on the bottom line as opposed to the public welfare. Government must step in, not by reducing taxes, which will only increase profits at the expense of labor, but by being the employer of last resort in hopefully a productive way.

Populism is on the march and a Trump victory will do little to halt its advance in future decades. If anything, it is demographically baked in the cake. Investors, as *The Economist* astutely pointed out, face a possible no-win situation. Unless the worker's share of GDP reverses its downward trend, and capital's share peaks, then populists worldwide will reject establishment parties in almost every future election – initiating in some cases growth-negative policies revolving around trade, immigration, and yes, in Trump's case, lower taxation that may lower GDP growth, not raise it. Global populism is the wave of the future, but it has taken a wrong turn in America. Investors must drive with caution, understanding that higher deficits resulting from lower taxes raise interest rates and inflation, which in turn have the potential to produce lower earnings and P/E ratios. There is no new Trump bull market in the offing. Be satisfied with 3-5% globally diversified returns. The Wall Street, finance-led hegemon is fading. The Populist sunrise has barely broken the horizon.

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